losses were effectively connected for such year with the conduct of a trade or business in the United States by such individual. However, in determining such excess of gains over losses no deduction may be taken under section 1202, relating to the deduction for capital gains, or section 1212, relating to the capital loss carryover. Thus, for example, in determining such excess gains all amounts considered under chapter 1 of the Code as gains or losses from the sale or exchange of capital assets shall be taken into account, except those gains which are described in section 871(a)(1) (B) or (D) and taken into account under paragraph (c) of this section and are considered to be gains from the sale or exchange of capital assets. Also, for example, a loss described in section 631 (b) or (c) which is considered to be a loss from the sale of a capital asset shall be taken into account in determining the excess gains which are subject to tax under this paragraph. In further illustration, in determining such excess gains no deduction shall be allowed, pursuant to the provisions of section 267, for losses from sales or exchanges of property between related taxpayers. Any gains which are taken into account under section 871(a)(1) and paragraph (c) of this section shall not be taken into account in applying section 1231 for purposes of this paragraph. Gains and losses are to be taken into account under this paragraph whether they are short-term or long-term capital gains or losses within the meaning of section 1222.

(ii) *Gains not included.* The provisions of this paragraph do not apply to any gains described in section 871(a)(1) (B) or (D), and in subdivision (i), (iii), or (iv) of paragraph (c)(1) of this section, which are considered to be gains from the sale or exchange of capital assets.

(iii) *Allowance of losses.* In determining the excess of gains over losses subject to tax under this paragraph losses shall be allowed only to the extent provided by section 165(c). Losses from sales or exchanges of capital assets in excess of gains from sales or exchanges of capital assets shall not be taken into account.

(e) *Credits against tax.* The credits allowed by section 31 (relating to tax withheld on wages), by section 32 (relating to tax withheld at source on nonresident aliens), by section 39 (relating to certain uses of gasoline and lubricating oil), and by section 6402 (relating to overpayments of tax) shall be allowed against the tax of a nonresident alien individual determined in accordance with this section.

(f) *Effective date.* Except as otherwise provided in this paragraph, this section shall apply for taxable years beginning after December 31, 1966. Paragraph (b)(2) of this section is applicable to payments made after November 13, 1997. For corresponding rules applicable to taxable years beginning before January 1, 1967, see 26 CFR 1.871–7 (b) and (c) (Revised as of January 1, 1971).

[T.D. 7332, 39 FR 44219, Dec. 23, 1974, as amended by T.D. 8734, 62 FR 53416, Oct. 14, 1997; T.D. 8735, 62 FR 53501, Oct. 14, 1997]

§ 1.871–8 Taxation of nonresident alien individuals engaged in U.S. business or treated as having effectively connected income.

(a) *Segregation of income.* This section applies for purposes of determining the tax of a nonresident alien individual who at any time during the taxable year is engaged in trade or business in the United States. It also applies for purposes of determining the tax of a nonresident alien student or trainee who is deemed under section 871(c) and §1.871–9 to be engaged in trade or business in the United States or of a nonresident alien individual who at no time during the taxable year is engaged in trade or business in the United States but has an election in effect for the taxable year under section 871(d) and §1.871–10 in respect to real property income. A nonresident alien individual to whom this section applies must segregate his gross income for the taxable year into two categories, namely (1) the income which is effectively connected for the taxable year with the conduct of a trade or business in the United States by that individual, and (2) the income which is not effectively connected for the taxable year with the conduct of a trade or business in the United States by that individual. A separate tax shall then be determined upon each such category of income, as provided in paragraph (b) of this section. The determination of

whether income or gain is or is not effectively connected for the taxable year with the conduct of a trade or business in the United States by the nonresident alien individual shall be made in accordance with section 864*(c)* and §§1.864–3 through 1.864–7. For purposes of this section income which is effectively connected for the taxable year with the conduct of a trade or business in the United States includes all income which is treated under section 871 (c) or (d) and §1.871–9 or §1.871–10 as income which is effectively connected for such year with the conduct of a trade or business in the United States by the nonresident alien individual.

(b) *Imposition of tax*—(1) *Income not effectively connected with the conduct of a trade or business in the United States.* If a nonresident alien individual who is engaged in trade or business in the United States at any time during the taxable year derives during such year from sources within the United States income or gains described in section 871(a)(1), and paragraph (b) or (c) of §1.871–7 or gains from the sale or exchange of capital assets determined as provided in section 871(a)(2) and paragraph (d) of §1.871–7, which are not effectively connected for the taxable year with the conduct of a trade or business in the United States by that individual, such income or gains shall be subject to a flat tax of 30 percent of the aggregate amount of such items. This tax shall be determined in the manner, and subject to the same conditions, set forth in §1.871–7 as though the income or gains were derived by a nonresident alien individual not engaged in trade or business in the United States during the taxable year, except that (i) the rule in paragraph (d)(3) of such section for treating the calendar year as the taxable year shall not apply and (ii) in applying paragraph (c) and (d)(4) of such section, there shall not be taken into account any gains or losses which are taken into account in determining the tax under section 871(b) and subparagraph (2) of this paragraph. A nonresident alien individual who has an election in effect for the taxable year under section 871(d) and §1.871–10 and who at no time during the taxable year is engaged in trade or business in the United States must determine his tax under §1.871–7 on his income which is not treated as effectively connected with the conduct of a trade or business in the United States, subject to the exception contained in subdivision (ii) of this subparagraph.

(2) *Income effectively connected with the conduct of a trade or business in the United States*—(i) *In general.* If a nonresident alien to whom this section applies derives income or gains which are effectively connected for the taxable year with the conduct of a trade or business in the United States by that individual, the taxable income or gains shall, except as provided in §1.871–12, be taxed in accordance with section 1 or, in the alternative, section 1201(b). See section 871(b)(1). Any income of the nonresident alien individual which is not effectively connected for the taxable year with the conduct of a trade or business in the United States by that individual shall not be taken into account in determining either the rate or amount of such tax. See paragraph (b) of §1.872–1.

(ii) *Determination of taxable income.* The taxable income for any taxable year for purposes of this subparagraph consists only of the nonresident alien individual's taxable income which is effectively connected for the taxable year with the conduct of a trade or business in the United States by that individual; and, for this purpose, it is immaterial that the trade or business with which that income is effectively connected is not the same as the trade or business carried on in the United States by that individual during the taxable year. See example 2 in §1.864–4(b). In determining such taxable income all amounts constituting, or considered to be, gains or losses for the taxable year from the sale or exchange of capital assets shall be taken into account if such gains or losses are effectively connected for the taxable year with the conduct of a trade or business in the United States by that individual, and, for such purpose, the 183-day rule set forth in section 871(a)(2) and paragraph (d)(2) of §1.871–7 shall not apply. Losses which are not effectively connected for the taxable year with the conduct of a trade or business

in the United States by that individual shall not be taken into account in determining taxable income under this subdivision, except as provided in section 873(b)(1).

(iii) *Cross references.* For rules for determining the gross income and deductions for the taxable year, see sections 872 and 873, and the regulations thereunder.

(c) *Change in trade or business status*—(1) *In general.* The determination as to whether a nonresident alien individual is engaged in trade or business within the United States during the taxable year is to be made for each taxable year. If at any time during the taxable year he is engaged in a trade or business in the United States, he is considered to be engaged in trade or business within the United States during the taxable year for purposes of sections 864(c)(1) and 871(b), and the regulations thereunder. Income, gain, or loss of a nonresident alien individual is not treated as being effectively connected for the taxable year with the conduct of a trade or business in the United States if he is not engaged in trade or business within the United States during such year, even though such income, gain, or loss may have been effectively connected for a previous taxable year with the conduct of a trade or business in the United States. See §1.864–3. However, income, gain, or loss which is treated as effectively connected for the taxable year with the conduct of a trade or business in the United States by a nonresident alien individual will generally be treated as effectively connected for a subsequent taxable year if he is engaged in a trade or business in the United States during such subsequent year, even though such income, gain, or loss is not effectively connected with the conduct of the trade or business carried on in the United States during such subsequent year. This subparagraph does not apply to income described in section 871 (c) or (d). It may not apply to a nonresident alien individual who for the taxable year uses an accrual method of accounting or to income which is constructively received in the taxable year within the meaning of §1.451–2.

(2) *Illustrations.* The application of this paragraph may be illustrated by the following examples:

Example 1. B, a nonresident alien individual using the calendar year as the taxable year and the cash receipts and disbursements method of accounting, is engaged in business (business R) in the United States from January 1, 1971, to August 31, 1971. During the period of September 1, 1971, to December 31, 1971, B receives installment payments of $30,000 on sales made in the United States by business R during that year, and the income from sources within the United States for that year attributable to such payments is $7,509. On September 15, 1971, another business (business S), which is carried on by B only in a foreign country sells to U.S. customers on the installment plan several pieces of equipment from inventory. During the period of September 16, 1971, to December 31, 1971, B receives installment payments of $50,000 on these sales by business S, and the income from sources within the United States for that year attributable to such payments is $10,000. Under section 864(c)(3) and paragraph (b) of §1.864–4 the entire income of $17,500 is effectively connected for 1971 with the conduct of a business in the United States by B. Accordingly, such income is taxable to B under paragraph (b)(2) of this section.

Example 2. Assume the same facts as in example 1, except that during 1972 B receives installment payments of $20,000 from the sales made during 1971 in the United States by business R, and of $80,000 from the sales made in 1971 to U.S. customers by business S, the total income from sources within the United States for 1972 attributable to such payments being $13,000. At no time during 1972 is B engaged in a trade or business in the United States. Under section 864(c)(1)(B) the income of $13,000 for 1972 is not effectively connected with the conduct of a trade or business in the United States by B. Moreover, such income is not fixed or determinable annual or periodical income. Accordingly, no amount of such income is taxable to B under section 871.

Example 3. Assume the same facts as in example 2, except that during 1972 B is engaged in a new business (business T) in the United States from July 1, 1972, to December 31, 1972. Under section 864(c)(3) and paragraph (b) of §1.864–4, the income of $13,000 is effectively connected for 1972 with the conduct of a business in the United States by B. Accordingly, such income is taxable to B under paragraph (b)(2) of this section.

Example 4. Assume the same facts as in example 2, except that the installment payments of $20,000 from the sales made during 1971 in the United States by business R and not received by B until 1972 could have been received by B in 1971 if he had so desired.

Under §1.451–2, B is deemed to have constructively received the payments of $20,000 in 1971. Accordingly, the income attributable to such payments is effectively connected for 1971 with the conduct of a business in the United States by B and is taxable to B in 1971 under paragraph (b)(2) of this section.

(d) *Credits against tax.* The credits allowed by section 31 (relating to tax withheld on wages), section 32 (relating to tax withheld at source on nonresident aliens), section 33 (relating to the foreign tax credit), section 35 (relating to partially tax-exempt interest), section 38 (relating to investment in certain depreciable property), section 39 (relating to certain uses of gasoline and lubricating oil), section 40 (relating to expenses of work incentive programs), and section 6402 (relating to overpayments of tax) shall be allowed against the tax determined in accordance with this section. However, the credits allowed by sections 33, 38, and 40 shall not be allowed against the flat tax of 30 percent imposed by section 871(a) and paragraph (b)(1) of this section. Moreover, no credit shall be allowed under section 35 to a non- resident alien individual with respect to whom a tax is imposed for the taxable year under section 871(a) and paragraph (b)(1) of this section, even though such individual has income for such year upon which tax is imposed under section 871(b) and paragraph (b)(2) of this section. For special rules applicable in determining the foreign tax credit, see section 906(b) and the regulations thereunder. For the disallowance of certain credits where a return is not filed for the taxable year, see section 874 and §1.874–1.

(e) *Effective date.* This section shall apply for taxable years beginning after December 31, 1966. For corresponding rules applicable to taxable years beginning before January 1, 1967, see 26 CFR 1.871–7(d) (Revised as of January 1, 1971).

[T.D. 7332, 39 FR 44221, Dec. 23, 1974]

§ 1.871–9 Nonresident alien students or trainees deemed to be engaged in U.S. business.

(a) *Participants in certain exchange or training programs.* For purposes of §§1.871–7 and 1.871–8 a nonresident alien individual who is temporarily present in the United States during the taxable year as a nonimmigrant under subparagraph (F) (relating to the admission of students into the United States) or subparagraph (J) (relating to the admission of teachers, trainees, specialists, etc., into the United States) of section 101(a)(15) of the Immigration and Nationality Act (8 U.S.C. 1101(a)(15) (F) or (J)), and who without regard to this paragraph is not engaged in trade or business in the United States during such year, shall be deemed to be engaged in trade or business in the United States during the taxable year. For purposes of determining whether an alien who is present in the United States on an F visa or a J visa is a resident of the United States, see §§301.7701(b)–1 through 301.7701(b)–9 of this chapter.

(b) *Income treated as effectively connected with U.S. business.* Any income described in paragraph (1) (relating to the nonexcluded portion of certain scholarship or fellowship grants) or paragraph (2) (relating to certain nonexcluded expenses incident to such grants) of section 1441(b) which is received during the taxable year from sources within the United States by a nonresident alien individual described in paragraph (a) of this section is to be treated for purposes of §§1.871–7, 1.871–8, 1.872–1, and 1.873–1 as income which is effectively connected for the taxable year with the conduct of a trade or business in the United States by that individual. However, such income is not to be treated as effectively connected for the taxable year with the conduct of a trade or business in the United States for purposes of section 1441(c)(1) and paragraph (a) of §1.1441–4. For exclusion relating to compensation paid to such individual by a foreign employer, see paragraph (b) of §1.872–2.

(c) *Exchange visitors.* For purposes of paragraph (a) of this section a nonresident alien individual who is temporarily present in the United States during the taxable year as a nonimmigrant under subparagraph (J) of section 101(a)(15) of the Immigration and Nationality Act includes a nonresident alien individual admitted to the United States as an ''exchange visitor'' under section 201 of the U.S. Information and Educational Exchange